



**“The Law and Economics of Interchange”**

**Testimony of  
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**Before the Subcommittee on Commerce, Trade and Consumer  
Protection  
Committee on Energy and Commerce  
U.S. House of Representatives  
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**The Honorable Cliff Stearns (R-FL), Chairman  
The Honorable Janice D. Schakowsky (D-IL), Ranking  
Member**

Chairman Stearns, Ranking Member Schakowsky and Members of the subcommittee, I appreciate the opportunity to join you today to discuss the issue of interchange fees. My name is Karen Kerrigan, and I am President & CEO of the Small Business & Entrepreneurship Council (SBE Council), a nonprofit advocacy organization based in the nation's capital.

### **Caution on Price Controls as a Solution**

The SBE Council is dedicated to supporting policies and solutions that encourage entrepreneurship, small business growth, innovation and the vitality of the U.S. economy. As you are well aware, government or regulatory intervention often carries the possibility of unintended consequences. Small firms have experienced such fallout with respect to policy implementation in the areas of health care and taxation, to name two areas among many, which have imposed new burdens, generated inequities or constructed artificial barriers limiting growth opportunities.

That is why the SBE Council remains cautious and circumspect of solutions that call upon government to intervene in the workings of the marketplace. It is with that backdrop that we approach the issue of interchange fees and the call for price controls on such fees.

Do small business owners and SBE Council members like paying interchange fees? Of course not. They would much prefer that these costs were lower or non-existent, similar to other external costs such as electricity and rent. At the same time that they may bemoan paying these fees, most SBE Council members, as well as various small business

owners who have sent us comments on this issue, recognize that government regulation – whether directly, or through litigation -- has the potential to cause dislocation in a system that has generally served them well.

### **Acknowledging the Benefits of the Electronic Card Payments System**

Those prescribing price controls on interchange fees, I believe, have been remiss in not acknowledging the benefits that electronic payments (credit cards and other forms) have provided. For small firms, these benefits are numerous, including:

- Access to consumer purchasing power – increased sales.
- Rapid and certain payment.
- Reduced costs and headaches in dealing with bounced checks.
- Reduced worries and losses with respect to theft issues.
- Enabler of internet commerce – undeniably a boon to e-commerce start-ups, and “store-front expansion” for existing firms in penetrating new markets.
- Costs associated with billing, collections, and taking credits risks are circumvented.
- A compliment to the mix of other payment choices like checks and cash – increased choices for consumers.
- Improved efficiency.

The value that payment cards bring to each business owner varies depending upon his or her business, industry or situation. And, of course, if it is perceived or believed that electronic payment cards are not beneficial, business owners can simply refuse to take

payment in this form. Many small businesses are succeeding without utilizing payment cards.

### **Government or Legal Intervention Will Have Consequences: Small Businesses**

#### **Express Concern**

No one can disagree that small businesses, like all parties, have a major stake in the ongoing success, efficiency and development of the electronic payments system.

Of course, it makes sense that retailers wish to reduce costs. However, as with other price control schemes that have been attempted in the past, incentives to invest and innovate are greatly diminished, which would not bode well for the enhancement, expansion, and maintenance of an extraordinarily complex payments system.

In addition, if incentives to widely market credit or payment cards are diminished, or if cardholders are faced with added costs or fewer benefits, that means a reduction in the use of cards. This will not be a positive development for small business owners either.

With respect to the SBE Council's concern over the unintended consequences of government intervention, or court-ordered solutions, that aim to set interchange fees, small firms throughout the nation share our apprehension as well. While, certainly, there are small businesses that would welcome intervention in this area (as long government or the courts do not tell them how to set prices, or run their businesses), others are more wary of such action. Here are just a few examples of the communications the SBE Council has received regarding this contentious issue:

***Electronic Payments Fueled e-Commerce, Free Enterprise System Works Fine***

“It’s undeniable that the electronic payments made possible by credit cards have revolutionized retail sales. Without them, the incredible boom in e-commerce would almost certainly never have happened. Interchange fees are necessary to fund the expansion of electronic payments into new merchant venues, as well as the development of new products that will help buyers and sellers alike. Merchants derive many benefits from accepting credit cards – more customers, more sales and fewer hassles connected with getting paid. Credit cards are a perfect example of the free enterprise system at work, and we shouldn’t bother it while it’s working.”

**Larry Romero, Target Strategies, LLC, South Bend, IN**

***Courtroom or Boardroom?***

“My company, Visionary Sports, operates on-line and we require payment by credit card. The system we have now works pretty well and is too valuable to our nation’s business community to tinker with. If a company feels like the interchange fee is too high, they can always stop accepting the cards (although I doubt many of them would want to). No one is forcing me to accept credit cards. I just think it’s the easiest and most cost effective way for my company to conduct business. If I change my mind at some point I’ll simply stop accepting them, I won’t need a judge to make that decision for me. The government does set prices in some countries, but America isn’t one of them and I hope it never will be. This is a poorly thought out plan that could start us down the road to a time when

prices will be negotiated in the courtroom instead of the conference room. I don't think any of us want to go there."

**Rodney Grubbs, Visionary Sports, Brookville, IN**

***We Can Handle Pricing Issues***

"Do I wish the fees were lower? Oh sure, the same as I wish my electric bill was smaller. But I understand that businesses need to charge for their services and I'm okay with that. As you can imagine, payment is a serious issue for us and we have found credit cards to be an extremely useful tool. With credit cards we're assured of payment, never have to deal with collection agencies and don't even have to generate an invoice. The fees charged by the credit card companies are worth the advantages we gain from their use. One of the things that make this country great is the chance everyone has to make their own decisions and run their affairs as they see fit. I hope the courts remember that and leave pricing issues up to the business community. We can handle it."

**Peter Gavin, Polylok, Wallingford, CT**

***No One is Forcing Us to Take Credit or Payments Card: We Can Make Own Decisions***

"My family has operated the Adams Pecan Company in Union Springs for over 60 years. I'm the third generation in the business and there's a fourth right behind me. These days our Alabama pecans are sold across the United States through our website. If the federal government sets an arbitrary limit on the fees card companies can charge, I fear it may make them less interested in promoting the use of their cards to new and existing customers. Fees are part of their profit structure and they need to make a profit to stay in

business. Just as I am free to set what I think is a reasonable price for our pecans, credit card companies should be able to set their own prices too. That's the way we do business in America. No one is making us deal with the card companies. We can make our own decisions."

**Kim Adams Graham, Adams Pecan, LLC, Union Springs, AL**

***Lawyers Win, We Lose***

"There's no reason for the courts to get involved in credit card interchange fees. The only time the legal system should get involved in pricing is when a monopoly exists in a particular market. That's not a problem in the credit card business; not only are there several card companies there are also other ways to get paid including debit cards, checks and cash. Retailers get a lot of benefit from accepting credit cards and forcing the card companies into court over fees seems pretty short-sighted. If the card companies aren't allowed to make a reasonable profit they'll probably cut back on incentive programs and usage rewards that help generate sales. These lawsuits – like so much litigation – will end up making a lot of money for the attorneys involved and not accomplishing much else."

**Ernie Del Giudice, MINUTEMAN PRESS, East Haven, CT**

**Conclusion**

As with a wide range of legislation or regulatory initiatives that Congress, regulatory agencies, and state and local officials will consider this year and beyond, the SBE Council will continue to implore that the "first do no harm" precept be followed. Particularly within the context of enabling our businesses, and those who support them,

to be more competitive in a global economy, intervening in an area where there is no market failure is indeed “pretty short-sighted.”

In the end, the SBE Council is very concerned that both consumers and small businesses will pay a price for government intervention. Litigation raises costs for everybody, and sets a precedent that will spread. When government, or the courts, sets prices, service inevitably suffers, including, in this case, fewer cards issued, consumer rewards reduced, and fees increased.

As SBE Council Raymond J. Keating wrote in a recent piece on interchange fees: “Fundamental economics must be kept in mind regarding interchange fees. Profits made by credit card companies encourage them to market, expand cardholders and merchants in the network, and accept credit risks, which in turn benefit both consumers and businesses. As with other businesses, credit card companies and banks have every incentive to get the price right for their services so as to maximize their profits. Set interchange fees too high and businesses will not accept the cards; set them too low and fewer cards are issued. Those prices and profits act as signals in the marketplace to spur competition and innovation.”

From the SBE Council’s perspective, the market has worked extraordinarily well in developing and sustaining a complex and secure payment system that everyone is benefiting from. Government intervention has generally proven to be costly and filled with unintended consequences, and therefore we are wary of efforts to impose an extreme



measure such as price controls on a system that has created significant benefits for small businesses and their customer base.

I look forward to your questions and our dialog on this important issue. Thank you Chairman Stearns, Ranking Member Schakowsky and members of the subcommittee for the opportunity to appear before you today.